

Message Text

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TO AMEMBASSY CANBERRA IMMEDIATE
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E.O. 11652: GDS

TAGS: EGEN

SUBJECT: US ECONOMIC SITUATION

REF: CANBERRA 2609

1. CANBERRA'S 2609 INDICATES SERIOUS MISPERCEPTION AT HIGH LEVELS OF AUSTRALIAN GOVERNMENT OF STATE OF US ECONOMY AND US ECONOMIC POLICY, FOR EXAMPLE, FOREIGN MINISTER PEACOCK'S REFERENCE TO A "US DEPRESSION." INFORMATION IS PROVIDED BELOW ON THESE MATTERS WHICH US EMBASSY SHOULD GIVE TO FOREIGN MINISTER TO CORRECT HIS MISPERCEPTIONS AND URGE HIM TO BRING TO THE ATTENTION OF THE PRIME MINISTER BEFORE PRIME MINISTER LEAVES FOR JAPAN.

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2. STATE OF US ECONOMY: SINCE THE SEVERE WORLD-WIDE RECESSION OF 1974-1975, THE US ECONOMY HAS BEEN EXPANDING AT A PACE ABOVE ITS LONG TERM POTENTIAL GROWTH. IN 1976 US REAL GNP GREW AT A 6 PERCENT RATE; IN 1977 IT GREW AT 4.9 PERCENT. OUTLOOK FOR 1978 IS FOR A REAL GROWTH RATE OF 4-5 PERCENT. RECOVERY IN MOST OTHER NATIONS HAS LAGGED FAR BEHIND OUR OWN. REAL GROWTH IN

THE EC LAST YEAR WAS LESS THAN 2 PERCENT AND IN JAPAN SLIGHTLY ABOVE 5 PERCENT. INDEED, A MAJOR REASON FOR THE

US TRADE DEFICIT LAST YEAR WAS THE SLOW GROWTH IN THE ECONOMIES OF OUR MAJOR TRADING PARTNERS.

3. UNEMPLOYMENT IN THE US, WHICH IN 1975 WAS 8.5 PERCENT OF THE CIVILIAN LABOR FORCE, IS CURRENTLY ABOUT 6.2 PERCENT. DURING THE COURSE OF OUR RECOVERY, WE HAVE MADE MORE PROGRESS THAN ANY OTHER INDUSTRIAL COUNTRY IN REDUCING UNEMPLOYMENT AND IDLE CAPACITY. IN 1977 ALONE, MORE THAN 4 MILLION NEW JOBS WERE CREATED IN OUR COUNTRY -- AN ALL-TIME RECORD -- AND UNEMPLOYMENT WAS REDUCED BY MORE THAN 1 MILLION PERSONS. UNEMPLOYMENT HAS DECLINED STILL FURTHER IN THE FIRST QUARTER OF 1978. MOREOVER, THE AFTER-TAX INCOME OF CONSUMERS, ADJUSTED FOR INFLATION, ROSE SUBSTANTIALLY IN 1977. WAGES OF THE TYPICAL AMERICAN WORKER INCREASED BY MORE THAN THE RISE OF PRICES, AND BUSINESS PROFITS ALSO ADVANCED.

4. OUR INFLATION RATE IS ALSO LOWER THAN IN MOST NATIONS. THE GNP IMPLICIT PRICE DEFLATOR WAS 5.3 PERCENT IN 1976, 5.5 PERCENT IN 1977. THE CONSUMER PRICE INDEX ROSE BY 4.8 PERCENT IN 1976 AND 6.8 PERCENT IN 1977, BUT THE ANNUAL RATE OF INCREASE IN THE NON-FOOD COMPONENT OF CONFIDENTIAL

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THE CONSUMER PRICE INDEX STILL REMAINS IN THE 6-6.5 PERCENT RANGE THAT HAS GENERALLY PREVAILED SINCE THE MIDDLE OF 1975.

5. THE PRESIDENT IN HIS ANTI-INFLATION SPEECH ON APRIL 11 MADE CLEAR HIS DETERMINATION TO CONTROL AND REDUCE THE RATE OF INFLATION WHICH, ALTHOUGH BETTER THAN IN MOST COUNTRIES, IS STILL TOO HIGH TO BE ACCEPTABLE. HE INTENDS TO MAINTAIN TIGHT CONTROL OVER THE GROWTH OF FEDERAL SPENDING, TO SECURE PASSAGE OF LEGISLATION TO CONTROL RISING COSTS IN SPECIFIC PROBLEM SECTORS SUCH AS HEALTH CARE, AND TO ENCOURAGE VOLUNTARY DECELERATION OF THE WAGE-PRICE SPIRAL.

6. THE RECENT DECLINE IN THE VALUE OF THE DOLLAR, PRIMARILY AGAINST THE CURRENCIES OF COUNTRIES IN STRONG TRADE AND CURRENT ACCOUNT SURPLUS, IS ATTRIBUTABLE TO OUR LARGE TRADE DEFICIT IN 1977 AND THEIR LARGE SURPLUSES. THE BASIC CAUSES OF THAT DEFICIT WERE THE GROWTH OF US PETROLEUM IMPORTS WHICH ROSE BECAUSE OF AN INCREASE IN PRICE AS WELL AS QUANTITY, AND THE FACT THAT WE HAVE BEEN GROWING FASTER THAN OUR TRADING PARTNERS. OUR STRONG

RECOVERY INCREASED DEMAND FOR IMPORTS WHILE THE SLOW GROWTH OF OUR TRADING PARTNERS SLOWED THE GROWTH OF OUR EXPORTS. FURTHERMORE, LAGGING BUSINESS INVESTMENT IN PLANT AND EQUIPMENT, WHICH HAS BEEN A MARKED FEATURE OF

THE POOR GROWTH PERFORMANCE IN OECD COUNTRIES, RETARDED DEMAND FOR US CAPITAL GOODS, WHICH CONSTITUTE ABOUT ONE-THIRD OF OUR TOTAL EXPORTS. AND WITH GOOD GRAIN HARVESTS AROUND THE WORLD, OUR FOOD AND FEED GRAIN EXPORTS DECLINED AS WELL.

7. IT SHOULD BE NOTED THAT THE RECENT DECLINE IN THE DOLLAR FOLLOWED A PERIOD OF ABOUT TWO AND ONE-HALF YEARS OF DOLLAR APPRECIATION. THE RESULT HAS BEEN THAT, AT
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THE PRESENT TIME (END OF MARCH 1978), THE DOLLAR HAD THE SAME VALUE VIS-A-VIS OECD CURRENCIES ON A TRADE-WEIGHTED BASIS AS IT HAD AT THE END OF 1974.

8. THE PRESIDENT IS DETERMINED TO REDUCE US DEPENDENCE ON IMPORTED OIL. AS HE MADE CLEAR IN HIS APRIL 11 SPEECH, SHOULD THE CONGRESS FAIL TO ACT ON HIS NATIONAL ENERGY PLAN, HE WILL TAKE ADMINISTRATIVE ACTION TO REDUCE OIL IMPORTS.

9. TO SUMMARIZE, THE US ECONOMY IS STRONG. THE PRESIDENT IS DETERMINED TO CONTINUE TO MOVE STEADILY TOWARD A HIGH EMPLOYMENT ECONOMY WHILE CONTAINING AND REDUCING THE RATE OF INFLATION AND DECREASING OUR EXCESSIVE DEPENDENCE ON IMPORTED OIL. WHILE DRAMATIC IMPROVEMENT IN THE US TRADE BALANCE THIS YEAR IS NOT EXPECTED, SOME IMPROVEMENT SHOULD OCCUR FROM THE GREATER CONVERGENCE OF GROWTH RATES IN THE OECD COUNTRIES, THE FREEZE ON OPEC OIL PRICES, AND THE POSITIVE EFFECT ON OUR TRADE BALANCE OF THE DOLLAR DEPRECIATION ALREADY EXPERIENCED. THE COMMITMENT OF JAPAN TO INCREASE DOMESTIC DEMAND IN ITS ECONOMY AND REDUCE ITS LARGE TRADE SURPLUS WILL BE AN IMPORTANT FACTOR IN THIS IMPROVEMENT, BENEFICIAL TO ALL TRADING NATIONS.

10. AS TO OUR INTERNATIONAL ECONOMIC POLICY, WE WILL CONTINUE TO COOPERATE CLOSELY WITH OTHER COUNTRIES TO:

-- PROMOTE CONTINUED ECONOMIC RECOVERY;

-- RESIST PROTECTIONIST PRESSURES;

-- REDUCE BARRIERS TO TRADE BY WORKING FOR A FAIR AND
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BALANCED AGREEMENT IN THE MTN IN WHICH JAPAN HAS AN
IMPORTANT ROLE TO PLAY;

-- ASSURE THAT ADEQUATE OFFICIAL FINANCING IS AVAILABLE,
IN CASE OF NEED, TO HELP COUNTRIES WITH SEVERE PAYMENTS
PROBLEMS ADOPT CORRECTIVE MEASURES;

-- CHECK DISORDERLY EXCHANGE RATE MOVEMENTS;

-- ENCOURAGE ENERGY CONSERVATION AND THE DEVELOPMENT OF
NEW SOURCES OF ENERGY; AND

-- INCREASE THE TRANSFER OF RESOURCES TO PROMOTE GROWTH
IN THE ECONOMIES OF THE DEVELOPING NATIONS. CHRISTOPHER

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